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Ratings

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Research Update:

Belgian Region of Brussels-Capital 'AA' Ratings Affirmed; Outlook Remains Stable

Primary Credit Analyst:
Loic Le Mercier, Paris (33) 1-4075-2563; loic.lemercier@spglobal.com

Secondary Contact:
Mehdi Fadli, Paris (33) 1-4420-6706; mehdi.fadli@spglobal.com

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Overview

- In 2017, thanks to its highly efficient financial management, the Belgian Region of Brussels-Capital posted stronger budgetary results than our previous base-case forecast.
- The region continues to maintain a very favorable liquidity situation.
- We are affirming our 'AA' long-term rating on Brussels-Capital.
- The stable outlook reflects our expectation that Brussels-Capital will continue to post a strong budgetary performance in 2018-2020, with limited deficits after capital accounts.

Rating Action

On March 23, 2018, S&P Global Ratings affirmed its 'AA' long-term issuer credit rating on Belgium's Region of Brussels-Capital. The outlook remains stable.

Outlook

The stable outlook reflects our base-case expectation that Brussels-Capital will maintain high operating performance and moderate deficits after capital accounts until 2020, while structurally posting a favorable liquidity position.

Downside scenario

We might consider a negative rating action in the next 24 months if we observe a structural deterioration in Brussels-Capital's budgetary performance, leading to rising debt. This could, for example, be due to the region's looser monitoring of government-related entities (GREs) that are within its consolidation scope or its unwillingness to use its own expenditure flexibility, showing a deterioration in its strict financial monitoring.

If we lowered our ratings on the Kingdom of Belgium (unsolicited AA/Stable/A-1+), or revised the outlook on Belgium to negative, we would take a similar action on Brussels-Capital. This is in accordance with our methodology for rating local and regional governments (LRGs) and their related sovereigns, under which we cap the long-term ratings and outlooks on Belgian LRGs at the level of those on the sovereign (see "Methodology: Rating Non-U.S.

Local And Regional Governments Higher Than The Sovereign," published Dec. 15, 2014, on RatingsDirect). In our view, Belgium's institutional and financial framework does not enable us to rate any Belgian LRGs above the sovereign.

Upside scenario

We could consider a positive rating action in the next 24 months if we took a similar action on Belgium, and if Brussels-Capital posted structural surpluses after capital accounts in 2018-2020, enabling it to structurally maintain tax-supported debt under 60% of consolidated operating revenues or its direct debt to operating balance below 3x.

Rationale

Our rating on Brussels-Capital primarily reflects our view of the region's tight financial management, with high sophistication and optimization in terms of debt, liquidity, and guarantee management. We believe the quality of management will enable the region to increase high investments over 2018-2020, while limiting debt accumulation and keeping its very favorable liquidity. We also think that the region will continue to benefit from a supportive institutional framework and a solid economy.

Financial management, the institutional framework, and the economy remain key strengths for Brussels-Capital

Brussels-Capital has an attractive and diversified economy, which translates into very high GDP per capita that we estimate at about €66,900 in 2017. Nevertheless, Brussels-Capital shows a less favorable socioeconomic profile than its international peers, with a structurally high unemployment rate well exceeding 15%, in spite of a positive trend in the past three years.

We consider that Brussels-Capital benefits from the maturity and stability of the institutional system for Belgian regions and communities, and a generally good revenue and expenditure balance. In our opinion, Belgium's sixth state reform--including the devolving of new responsibilities to regions and communities and greater financial autonomy to regions--has demonstrated the system's predictability. Institutional discussions on the reform started in 2007, but the budgetary effects were felt only from 2015. We think that the reform also illustrates the ability of Belgian LRGs to influence the central government's policy.

Brussels-Capital has shown its capacity to handle new responsibilities under the sixth state reform while keeping spending under control, thanks to its very strong financial management. We view positively the region's political and managerial strength, reliable budgeting, close oversight of intra-annual budget execution, prudent and sophisticated debt management, very efficient and optimized liquidity management, and close monitoring of GREs and other contingent risks, including its well-defined and active guarantee management system.

After a high surplus in 2017, we anticipate limited deficits, leading to low debt intake

In 2017, we estimate that the region outperformed our previous base-case forecast in terms of budgetary metrics. Its operating balance reached 17% of operating revenues (based on Brussels-Capital actual figures adjusted by S&P Global Ratings), versus 13% in our previous base-case scenario. This was mainly due to a decrease in its consolidated operating expenditures by more than 5% compared to 2016. Capital expenditure also reached lower levels than expected at €0.6 billion versus €1.1 billion in 2016. The fall in expenditure mainly happened at the GRE level--such as the municipality fund, Fonds régional bruxellois de refinancement des trésoreries communales (FRBRTC) and the employment office Actiris--but also reflected savings on Brussels-Capital's direct responsibilities (for example, on local entity funding). In our view, these improvements partly consist of one-off effects related to the enhanced economic context, and they may not repeat in 2018. Those developments allowed the region to post a high surplus after capital accounts of 8% of total revenues, while our previous base-case scenario anticipated a 2% deficit. However, we do not believe this surplus is structural or recurring, as we expect both operating and capital expenditure will recover in 2018 for the duration of our forecast.

From 2018 onward, we expect that Brussels-Capital will moderate growth of operating expenditure to about 2% annually (excluding the transfer of new responsibilities). Under our base-case scenario, we therefore anticipate a good consolidated operating surplus of 12% of consolidated operating revenues in 2020, which is in line with our former base case. In our forecast, we adjust for the property tax that the region starts to collect in 2018 on behalf of cities (estimated at €900 million) as we consider this a pass-through item.

We also expect that incurred capital expenditure will increase to about €1.3 billion annually in 2018-2020, at a slower pace than our previous base-case forecast of €1.4 billion. Therefore, we anticipate deficits after capital accounts will remain moderate, at about 4% of total revenues on average in 2018-2020.

To maintain good budgetary performance, we think that Brussels-Capital could use its average budgetary flexibility if needed. Its modifiable tax revenues, comprising the supplementary tax on personal income tax (PIT) and regional taxes, account for around 50% of its consolidated operating revenues. Still, we believe that Brussels-Capital would be less willing to tap its tax leeway and more likely to use its spending flexibility if needed, especially regarding capital expenditure, which we expect will account for 25% of total consolidated expenditures in 2018-2020.

Thanks to its strong budgetary performance, Brussels-Capital's consolidated tax-supported debt will likely only slightly increase to 101% of consolidated operating revenues in 2020, compared with 88% in 2016. Brussels-Capital's tax-supported debt includes the debt of the FRBRTC, which is fully consolidated under the European system of national and regional accounts 2010 (ESA 2010). FRBRTC lends the majority of its debt proceeds on to self-supporting municipalities in the region. This on-lent debt currently accounts for about 12% of Brussels-Capital's consolidated operating revenues.

Brussels-Capital currently benefits from a direct multiyear €1.5 billion account facility and FRBRTC also holds €225 million in liquidity lines. We expect the debt service coverage ratio to remain strong, with the amounts available under this account facility and the region's cash holdings covering far more than 120% of its consolidated debt service (including FRBRTC's short- and long-term debt repayments) in the next 12 months. In the next few months, the region is planning to reduce its direct multiyear account ceiling, but this will not affect its liquidity coverage, in our view. We also think that the region has strong access to external funding via the financial markets, especially through its medium-term note program, its Belgian commercial paper program, and its access to investors in Schuldschein loans.

We consider Brussels-Capital's contingent liabilities to be moderate. They mainly relate to the region's exposure to social housing mortgage companies, such as the Fonds du Logement de la Région de Bruxelles-Capitale, and a relatively financially weak municipal sector. In contrast with ESA 2010 treatment of social housing mortgage companies, we do not include their debt in the region's consolidated tax-supported debt, because we view them as self-supporting. The region's financial guarantees, mainly for social housing mortgage companies, accounted for about 30% of its consolidated operating revenues at year-end 2017. In assessing the region's contingent liabilities, we also factor in the financial situation of the municipal sector, which we view as having some weaknesses. We will also continue to monitor the potential risks that could emerge from the significant financial change faced by the public body, Commission Communautaire Commune, which saw its budget increase to nearly €1.3 billion in 2015 under the sixth state reform, from €100 million in 2014.

Key Statistics

Table 1

Region of Brussels-Capital Key Statistics

	--Fiscal year end Dec. 31--				
(Mil. €)	**2016**	**2017bc**	**2018bc**	**2019bc**	**2020bc**
Operating revenues	4,349	4,286	4,386	4,449	4,518
Operating expenditures	3,765	3,559	3,842	3,911	3,990
Operating balance	583	728	544	537	528
Operating balance (% of operating revenues)	13.4	17	12.4	12.1	11.7
Capital revenues	538	249	516	569	572
Capital expenditures	1,133	621	1,253	1,313	1,325
Balance after capital accounts	(12.0)	356.0	(193.0)	(207.0)	(224.0)
Balance after capital accounts (% of total revenues)	(0.2)	7.8	(3.9)	(4.1)	(4.4)

Table 1

Region of Brussels-Capital Key Statistics (cont.)					
	--Fiscal year end Dec. 31--				
(Mil. €)	**2016**	**2017bc**	**2018bc**	**2019bc**	**2020bc**
Debt repaid	649	681	627	721	690
Gross borrowings	601	498	720	928	914
Balance after borrowings	(59)	173	(100)	0	0
Modifiable revenues (% of operating revenues)	48.5	54.2	52.4	52	51.6
Capital expenditures (% of total expenditures)	23.1	14.9	24.6	25.1	24.9
Direct debt (outstanding at year-end)	3,842	4,046	4,139	4,346	4,570
Direct debt (% of operating revenues)	88.3	94.4	94.4	97.7	101.1
Tax-supported debt (outstanding at year-end)	3,873	4,075	4,169	4,376	4,600
Tax-supported debt (% of consolidated operating revenues)	89.1	95.1	95	98.4	101.8
Interest (% of operating revenues)	3.9	3.5	3.2	3.3	3.4
Local GDP per capita (€)	64,729	66,877	68,290	69,566	70,991
National GDP per capita (€)	37,545	38,718	39,843	40,903	42,064

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario.

Ratings Score Snapshot

Table 2

Region of Brussels-Capital Ratings Score Snapshot	
Key Rating Factors	
Institutionnal Framework	Very predictable and well-balanced
Economy	Strong
Financial Management	Very strong
Budgetary Flexibility	Average
Budgetary Performance	Strong
Liquidity	Exceptional
Debt Burden	Moderate
Contingent Liabilities	Moderate

*S&P Global Ratings' credit ratings on local and regional governments are based on eight main rating factors listed in the table above. Section A of S&P Global Ratings' "Methodology For Rating Non-U.S. Local And Regional Governments" summarizes how the eight factors are combined to derive the rating.

Key Sovereign Statistics

- Belgium 'AA/A-1+' Ratings Affirmed; Outlook Stable - Jan. 12, 2018

Related Criteria

- Criteria - Governments - International Public Finance: Methodology: Rating Non-U.S. Local And Regional Governments Higher Than The Sovereign, Dec. 15, 2014
- Criteria - Governments - International Public Finance: Methodology For Rating Non-U.S. Local And Regional Governments, June 30, 2014
- General Criteria: Ratings Above The Sovereign--Corporate And Government Ratings: Methodology And Assumptions, Nov. 19, 2013
- Criteria - Governments - International Public Finance: Methodology And Assumptions For Analyzing The Liquidity Of Non-U.S. Local And Regional Governments And Related Entities And For Rating Their Commercial Paper Programs, Oct. 15, 2009
- General Criteria: Use Of CreditWatch And Outlooks, Sept. 14, 2009
- Criteria - Governments - International Public Finance: Methodology And Assumptions: The Impact Of PPP Projects On International Local And Regional Governments: Refined Accounting Treatment, Dec. 15, 2008

Related Research

- Institutional Framework Assessments For Non-U.S. Local And Regional Governments - September 21, 2017
- Belgium 'AA/A-1+' Ratings Affirmed; Outlook Stable - Jan. 12, 2018
- 2016 Annual Non-U.S. Local And Regional Government Default Study And Rating Transitions - May 8, 2017

In accordance with our relevant policies and procedures, the Rating Committee was composed of analysts that are qualified to vote in the committee, with sufficient experience to convey the appropriate level of knowledge and understanding of the methodology applicable (see 'Related Criteria And Research'). At the onset of the committee, the chair confirmed that the information provided to the Rating Committee by the primary analyst had been distributed in a timely manner and was sufficient for Committee members to make an informed decision.

After the primary analyst gave opening remarks and explained the recommendation, the Committee discussed key rating factors and critical issues in accordance with the relevant criteria. Qualitative and quantitative risk factors were considered and discussed, looking at track-record and forecasts.

The committee agreed that all key rating factors were unchanged.

The chair ensured every voting member was given the opportunity to articulate his/her opinion. The chair or designee reviewed the draft report to ensure consistency with the Committee decision. The views and the decision of the rating committee are summarized in the above rationale and outlook. The weighting of all rating factors is described in the methodology used in this rating action (see 'Related Criteria and Research').

Ratings List

Ratings Affirmed

Brussels-Capital (Region of)	
Issuer Credit Rating	AA/Stable/--

Additional Contact:
SovereignEurope; SovereignEurope@spglobal.com